

January 4, 2001

MEMORANDUM FOR THE HEADS OF EXECUTIVE DEPARTMENTS AND
ESTABLISHMENTS, CHIEF FINANCIAL OFFICERS, AND INSPECTORS GENERAL

FROM: Joshua Gotbaum
Executive Associate Director and Controller

RE: **Revised Implementation Guidance for the Federal Financial Management
Improvement Act**

Attached is revised guidance for determining the compliance of financial systems with the Federal Financial Management Improvement Act (FFMIA) of 1996, Public Law 104-208, Title VIII (31 U.S.C. 3512 note). We have changed the guidance substantially, to focus agency and auditor activities on the essential requirements of FFMIA. The document lists the specific requirements of FFMIA, as well as factors to consider in reviewing systems for compliance. It also provides guidance to agency heads developing corrective action plans to bring an agency into compliance with FFMIA.

This guidance applies to those executive departments and agencies required to be audited and listed in Appendix A of OMB Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*. It applies immediately and should be used for financial reports and audits for fiscal year 2000 (unless your report and audit has already been completed) and thereafter.

We developed this guidance after consultation with agency CFO's and inspectors general. If you have questions or comments, please contact Joe Kull, Deputy Controller, at the Office of Federal Financial Management, (202) 395-3993.

This memorandum is also available at <http://www.whitehouse.gov/OMB/financial>.

Attachment

THE FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT OF 1996 OMB IMPLEMENTATION GUIDANCE

Introduction

The Federal Financial Management Improvement Act of 1996 (FFMIA), Public Law 104-208, Title VIII (31 U.S.C. 3512 note), was intended to advance Federal financial management by ensuring that Federal financial management systems can and do provide reliable, consistent disclosure of financial data, and that they do so on a basis that is uniform across the Federal government from year to year consistently using professionally-accepted accounting standards. This goes well beyond the requirements under the Government Management Reform Act (GMRA) that require agencies to publish annual audited financial reports. It is intended to provide the basis for ongoing use of reliable financial information in program management and in oversight by the President, the Congress and the public. Below are the requirements for FFMIA:

FFMIA fundamentally does three things:

- Establishes in statute certain financial management system requirements that are already Executive Branch policies. Specifically, section 803(a) of the FFMIA requires each agency to implement and maintain systems that comply substantially with:
 - (1) Federal financial management system requirements,
 - (2) applicable Federal accounting standards, and
 - (3) the Standard General Ledger (SGL) at the transaction level;
- Requires auditors to report on agency compliance with the three stated requirements as part of financial statement audit reports; and
- Requires agency heads to determine, based on the audit report and other information, whether their financial management systems comply with FFMIA. If they do not, agencies are required to develop remediation plans and file them with OMB.

The OMB Circular A-127, "Financial Management Systems," serves as a reference document for government-wide financial management systems. It prescribes policies and standards for agencies to follow in developing, operating, evaluating, and reporting on financial management systems. Charts 1-3 identify the applicable requirements from OMB Circular A-127, Section 7 that should be assessed when making an FFMIA compliance determination.

Some of the financial management systems requirements listed in Section 7 of Circular A-127, while important, are not essential to the particular requirements of FFMIA. As noted above, the Act was intended to ensure that agencies develop and use systems that generate reliable, timely and consistent information necessary for Federal managers' responsibilities. Agencies that can:

- Prepare financial statements and other required financial and budget reports using information generated by the financial management system(s);
- Provide reliable and timely financial information for managing current operations;
- Account for their assets reliably, so that they can be properly protected from loss, misappropriation, or destruction; and
- Do all of the above in a way that is consistent with Federal accounting standards and the Standard General Ledger are substantially compliant with FFMIA.

In determining whether an agency's financial management systems substantially comply with FFMIA, management and auditors need to consider whether a system's performance prevents the agency from meeting the specific requirements of FFMIA as listed above. Identified deficiencies that do not prevent the agency from meeting the above requirements generally should not be considered as part of a FFMIA compliance determination. Auditors then need to use judgment in assessing whether the adverse impacts caused by identified deficiencies are instances of substantial noncompliance with FFMIA.

This Act applies only to entities listed in Appendix A of OMB Bulletin 01-02, and subsequent issuances.

Statutory Procedural Requirements of FFMIA

General

The FFMIA does not itself establish any new financial system requirements. However, it does establish a statutory requirement for agency-heads to assess, on an annual basis, whether their financial management systems comply with the three requirements of FFMIA. Agencies that are not in substantial compliance with FFMIA must develop remediation plans to achieve compliance. It also requires an auditor to report on agency compliance with FFMIA as part of the annual financial statement audit process.

Agency Responsibilities

- **Determining Compliance.** Section 803(c)(1) of the FFMA requires the head of each agency to make a determination of the agency's substantial compliance with Section 803(a) of the Act, based upon a review of the auditor's report and any other information the head of the agency considers relevant and appropriate. The agency-head's determination of substantial compliance is due to OMB no later than 120 days after receipt of an agency-wide audited financial statement (generally due March 1 of the following fiscal year); or, if earlier, 120 days after the end of the fiscal year following the year covered by such statement.
- **Developing Remediation Plans if Non-Compliant.** Section 803(c)(3) of the FFMA requires that:
 1. If the head of an agency determines that the agency's financial management systems do not substantially comply with the requirements of the Act, a remediation plan must be developed, in consultation with OMB, that describes the resources, remedies, and milestones for achieving substantial compliance. The format of a remediation plan is explained in OMB Circular A-11.

Agency heads are responsible for agency progress towards resolving identified deficiencies and such progress should be discussed in the agency's remediation plan, capital planning and investment control plans, and other planning documents, when applicable. When discussing resolution of deficiencies in such reports, the findings or analysis of noncompliance should be included with a discussion of ongoing remediation activities. Progress towards resolving the deficiencies should not be construed as compliance with FFMA
 2. If the determination by the head of the agency differs from the audit compliance findings (required as part of the financial statement audit), the agency must notify OMB explaining the differences. The Director of OMB shall review such determinations and provide a report on the findings to the appropriate committees of the Congress.
 3. Generally, a remediation plan is expected to bring the agency's financial management systems into substantial compliance no later than three years after the date a determination is made by the head of the agency. If, however, the agency (in concurrence with OMB) determines that the agency's financial management systems cannot be brought into substantial within 3 years, the agency may specify a longer period. In this case, the agency must designate an agency official responsible for bringing the agency's financial management systems into substantial compliance by the date specified.

Auditor Responsibilities

- **Reporting on Compliance.** Section 803(b)(1) of the FFMIA requires that auditors report on FFMIA compliance as part of the financial statement audit process based upon OMB's Audit Bulletin (Bulletin 01-02, and subsequent issuances).
- Where an agency's systems are considered not substantially compliant, Section 803(b)(2) specifically requires that the auditor discuss in the audit report:
 1. the entity or organization responsible for the financial management systems that have been found not to comply;
 2. all facts pertaining to the failure to comply with the requirements;
 3. the nature and extent of the noncompliance including areas in which there is substantial but not full compliance;
 4. the primary reason or cause of the noncompliance;
 5. any relevant comments from any responsible official; and,
 6. recommended remedial actions and the time frames to implement such actions.

To meet these reporting requirements, auditors need to plan and perform their audit work in sufficient detail to enable them to determine the degree of compliance and report on instances of noncompliance for all of the applicable requirements. By providing this level of detail, the auditor can constructively assist management to bring about needed changes in an agency's financial management system.

Auditors should also report on agency progress in achieving FFMIA compliance. If agencies have reduced the degree of noncompliance from the previous reporting period, the auditor's report should include a discussion of the improvements as well acknowledge ongoing agency efforts to strengthen financial management systems.

- **Reporting on Failure to Meet Deadlines in Remediation Plans.** Section 804(b) of the FFMIA requires that the Inspector General's (IG) semi-annual report to Congress required under section 5(a) of the Inspector General Act of 1978, as amended, include instances and reasons when an agency has not met the milestones established in the remediation plan. Specifically, the report shall include:

1. the facts pertaining to non-compliance with Section 803 (a), including the nature and extent of non-compliance, the primary reason or cause for the failure to comply, and any extenuating circumstances;
2. a statement of the remedial actions needed to comply; and
3. the entity or organization responsible for the noncompliance and if different, the entity or organization responsible for correcting the non-compliance;

In addition to these reporting requirements, both OMB and GAO have annual reporting requirements under the Act.

Factors to Consider in Determining Compliance

Applicability

Federal agencies must comply, and agency auditors must report whether the agency's financial management systems substantially comply, with applicable financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger. FASAB standards incorporated in OMB's Bulletin, *Form and Content*, are the applicable accounting standards for the Federal government. OMB Circular A-127 is the source of Federal financial management systems requirements. While all of the financial management systems requirements listed in Section 7 of Circular A-127 are important, some of the Section 7 requirements are not essential to satisfying the particular requirements of FFMIA, and to the ability of an agency's financial management systems to generate reliable, timely, and consistent information necessary for Federal managers' responsibilities.

Chart 1 identifies the specific Federal financial management systems requirements from Circular A-127 that should be met; Chart 2, the applicable Federal accounting standards; and Chart 3, compliance with the Standard General Ledger (SGL) at the transaction level. Each chart also includes performance indicators that should be helpful when making an FFMIA compliance determination.

Assessing the Impact of Instances of Noncompliance with FFMIA Requirements

In determining whether instances of noncompliance with the requirements listed in Charts 1 through 3 would result in systems not being substantially compliant with FFMIA as a whole, management and auditors need to assess the impact of the instance of noncompliance identified. Agencies that can:

- Prepare financial statements and other required financial and budget reports using information generated by the financial management system(s);
- Provide reliable and timely financial information for managing current operations;

- Account for their assets reliably, so that they can be properly protected from loss, misappropriation, or destruction; and
- Do all of the above in a way that is consistent with Federal accounting standards and the Standard General Ledger are substantially compliant with FFMIA.

Meeting Minimum Standards versus Achieving Ideal Performance

Ideally, financial management systems should provide complete, reliable, timely and useful financial management information efficiently and automatically. However, FFMIA compliance itself neither requires nor results in ideal or state-of-the-art system performance or system efficiency; nor does it require that systems be entirely automated. What FFMIA compliance indicates is that systems routinely provide reliable financial information consistently, accurately, and reported uniformly. The charts, included in this document, both describe the requirements and provide examples of indicators for compliance.

Specific FFMIA Requirements and Compliance Indicators (Charts 1-3)

The charts that follow are intended to help provide guidance on each of the FFMIA requirements. Each chart describes both (a) the minimum requirements to achieve compliance, as well as (b) examples of measures and indicators of compliance with those requirements.

In reviewing the following charts it is important to note that not every "requirement" or compliance indicator is applicable to every agency. The agency must first determine whether a particular requirement is relevant to the agency's financial management system as described above. Once an activity is considered applicable to an agency's financial system, then the agency should determine whether its financial management system can perform the activity and meet the requirement.

The indicators found on the following charts are provided as examples, not requirements. The indicators are intended to be both broad and flexible and to provide a practical basis for measuring substantial compliance with the FFMIA requirements. An agency head may make a determination of "substantial compliance" without satisfying every indicator.

Chart 1. Financial Systems Requirements

Requirements	Indicators of Compliance
<p>Agency financial management systems shall comply with the following requirements identified and discussed in further detail in OMB Circular A-127, Section 7:</p> <ul style="list-style-type: none"> • Agency-wide Financial Information Classification Structure: <ul style="list-style-type: none"> --shall be consistent with SGL; --shall track program expenditures; and --shall ensure consistent data in budget accounting and financial reports. • Integrated Financial Management Systems: <ul style="list-style-type: none"> --shall provide interrelationships between the core financial system and feeder systems (whether automated or not); --shall establish common data elements (definitions and formats) to record financial events throughout the financial system and ensure it is collected, stored and retrieved in the common standard format; --shall incorporate Government-wide standards and external reporting requirements into the standard data classification structure; --shall consistently process common transactions throughout the financial system (manual and automated); and --shall use and apply consistently internal controls throughout the financial system. 	<ol style="list-style-type: none"> 1. Documentation from reviews of financial systems describe how requirements, found in OMB Circular A-127 that are considered applicable, have been implemented. To assist in reviews of financial management systems under FFMIA, JFMIP literature and other checklists are available that can be used as practice aids to help determine whether specific functional requirements are being met. <p>Some example attributes that serve as indicators of compliance as a result of a systematic review of core and feeder systems include the following:</p> <ol style="list-style-type: none"> a. User access controls/passwords and user authorizations are authorized in writing and implemented and other financial controls are in place and operating effectively; b. Budget execution is integrated in the core financial system with accounts payable, accounts receivable and general ledger; c. Users have on-line access to the status of funds or receive daily reports on the status of funds to perform analyses or decision making; d. Prior to processing transactions, users are notified that an obligation or expenditure would exceed funds available, or an expenditure exceeds the amount of an obligation established for that purpose; e. Feeder systems are integrated or electronically interfaced with the core financial system; f. A common accounting classification structure is used; g. An audit trail exists from any summary data recorded in the core financial system to detailed source transactions maintained in feeder systems; h. Information on approved and disapproved direct loans is maintained; i. Employee compensation is initiated, maintained, and reported correctly and timely; j. The status and disposition of inventory items are maintained; k. Debt referred for collection or offset by Federal collections is identified; and l. Interest on overdue payments and discounts is calculated.

<ul style="list-style-type: none"> • Financial Reporting: --shall comply with internal and external reporting requirements, including financial statement preparation. • Budget Reporting: --shall ensure the agency' financial management system supports the preparation, execution and reporting of the agency's budget in accordance with OMB Circular No. A-11 (Preparation and Submission of Budget Estimates) and OMB Circular No. A-34 (Instructions on Budget Execution) and other OMB circulars and bulletins and --shall support budget formulation and execution functions. • Security: --shall ensure security over financial management information systems in accordance with OMB Circular A-130, Appendix 3, Section 3, Automated Information Security Programs dated Feb. 8, 1996. 	<p>2. The agency can produce auditable financial statements based on the data from the agency's financial system and provide reliable financial information for managing current government operations and preparing financial reports.</p> <p>3. Existing reviews and audits required by A-130, Appendix 3, do not disclose material deficiencies. Specifically, for financial management systems, the following are present:</p> <ul style="list-style-type: none"> a. Assignment of security responsibilities; b. Implementation of a system security plan; c. Review of security controls; and d. Authorization for processing.

Chart 2. Accounting Standards

Requirements	Indicators of Compliance
<p>An agency's financial management systems are considered in substantial compliance with Federal accounting standards, as defined by OMB, if:</p> <ul style="list-style-type: none"> the agency's financial statements are compiled in accordance with the Federal accounting standards prescribed by OMB's Form and Content Bulletin (OMB Bulletin 97-01, as amended and successor documents); and financial information used for internal management is accurate and consistent with Federal accounting standards that are applicable and that are in effect for the period that the financial report/ covers. 	<ol style="list-style-type: none"> 1. An unqualified opinion, or a qualified opinion or disclaimer issued by the auditor for reasons other than the agency's ability to prepare auditable financial statements. For instance, an opinion or disclaimer by result from a material uncertainty, such as resolution of litigation or projecting future economic events, and not from the failure to implement applicable accounting standards; and 2. The audit disclosed no material weaknesses in internal control that affect the agency's ability to prepare financial statements and related disclosures, budget reports, or other financial information for agency management decision-making purposes that are consistent with the Federal accounting standards; and 3. The agency produces managerial cost information consistent with standards in SFFAS4.

Chart 3. Standard General Ledger at the Transaction Level

Requirements	Indicators of Compliance
<p>Substantial compliance with the SGL at the transaction level requires the agency's recording of financial events to be consistent with all applicable account descriptions and posting models/attributes reflected in the Standard General Ledger issued by the Financial Management Service, Department of the Treasury, are effective for the period covered by the audit.</p> <p>Implementing the SGL at the transaction level requires that:</p> <ul style="list-style-type: none"> • transactions are recorded in full compliance with the SGL Chart of Account's descriptions and posting models/attributes that demonstrate how the SGL is to be used for recording transactions of the Federal government accounting process; • reports produced by the systems provide financial information, whether used internally or externally, that can be traced directly to the SGL accounts; • transactions from feeder systems, which may be summarized and interfaced into the core financial system's general ledger, are posted following SGL requirements. 	<ol style="list-style-type: none"> 1. A report or on-site demonstration of the financial system identifies the posting models (debit and credit pairs) and attributes which are used to record financial events, and ensures the posting models and attributes are consistent with those in the Standard General Ledger; 2. If transactions from feeder systems are summarized before recording in the core financial system, then an on-site feeder demonstration or report indicates that transactions are recorded in the manner consistent with the account definitions, posting models/attributes specified in the SGL and are traceable to source documents; and 3. If transactions are posted directly to the core financial system, then, transactions are traceable to source documents. <p align="center">OR</p> <ol style="list-style-type: none"> 1. If a system is using crosswalk tables, then a system report or on-site demonstration identifies alternative codes (pseudo-code) that are used to record financial events and follows the same account descriptions and posting models/attributes that are reflected in the SGL; 2. Financial data produced can be directly and appropriately matched to SGL codes for reporting to OMB and Treasury and for preparing financial statements. The use of the SGL code in the feeder system is not necessary as long as the code definitions used to capture information are consistent with the SGL definitions; and 3. If transactions from feeder systems are summarized before recording in the core financial system, then an on-site feeder system demonstration or feeder system generated report indicates that transactions are recorded in a manner consistent with the account definitions, posting models/attributes specified in the SGL and are traceable to source documents.